

Audit Report



FY 1997 FINANCIAL REPORTING BY
THE DEFENSE AUTOMATED PRINTING SERVICE

Report No. 98-201

September 23, 1998

Office of the Inspector General
Department of Defense

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Acronyms

DAPS	Defense Automated Printing Service
DBOF	Defense Business Operations Fund
DFAS	Defense Finance and Accounting Service
DLA	Defense Logistics Agency
DWAS	Defense Working Capital Fund Accounting System
GAO	General Accounting Office
IG	Inspector General
KAR	Key Accounting Requirement
OMB	Office of Management and Budget
PRMIS	Printing Resource Management Information System
SGL	Standard General Ledger
USGSL	U.S. Government Standard General Ledger
WCF	Working Capital Fund



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
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ARLINGTON, VIRGINIA 22202

September 23, 1998

MEMORANDUM FOR DIRECTOR, DEFENSE FINANCE AND ACCOUNTING
SERVICE
DIRECTOR, DEFENSE LOGISTICS AGENCY
DIRECTOR, DEFENSE AUTOMATED PRINTING
SERVICE

SUBJECT: Audit Report on FY 1997 Financial Reporting by the Defense Automated
Printing Service (Report No. 98-201)

We are providing this report for review and comments. The Defense Finance and Accounting Service did not comment to a draft of this report. Management comments received from Defense Logistics Agency conformed to the requirements of DoD Directive 7650.3; therefore, additional Defense Logistics Agency comments are not required. DoD Directive 7650.3; requires that all recommendations be resolved promptly. We request that the Director, Defense Finance and Accounting Service provide comments on the final report by November 23, 1998.

Management comments should indicate concurrence or nonconcurrence with the finding and each applicable recommendation. Comments should describe the corrective actions taken or planned in response to agreed-upon recommendations and should designate the completion date of the action. State specific reasons for any nonconcurrence and propose alternative actions, if appropriate.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Mr. James L. Kornides or Mr. Stuart D. Dunnett at (614) 751-1400, e-mail jkornides@dodig.osd.mil or sdunnett@dodig.osd.mil. See Appendix B for the report distribution. A list of audit team members is on the inside back cover.

A handwritten signature in cursive script, reading "David K. Steensma", is positioned above the typed name.

David K. Steensma
Deputy Assistant Inspector General
for Auditing

Office of the Inspector General, DoD

Report No. 98-201
(Project No. 8FJ-2002.04)

September 23, 1998

FY 1997 Financial Reporting by the Defense Automated Printing Service

Executive Summary

Introduction. The audit was performed to meet the requirements of Public Law 101-576, the "Chief Financial Officers Act of 1990," as amended by Public Law 103-356, the "Federal Financial Management Act of 1994." This report is the fifth in a series of reports resulting from our audit of the FY 1997 Defense Logistics Agency Working Capital Fund financial statements. Appendix A lists the two reports in the series that have been issued as final reports.

On October 1, 1996, the Defense Automated Printing Service became a separate business area within the Defense Logistics Agency Defense Working Capital Fund to consolidate printing, duplicating, and document automation resources for the DoD. Prior to FY 1997, the Defense Automated Printing Service was a Navy administered activity of the Defense Business Operations Fund. For FY 1997, the Defense Automated Printing Service reported \$399.9 million in revenue and \$388.0 million in expenses.

The Defense Finance and Accounting Service (DFAS) provides accounting services for the Defense Automated Printing Service. The accuracy of information in the financial systems and reported on financial statements is the joint responsibility of the Defense Automated Printing Service and the Defense Logistics Agency. Preparation of the financial statements is the joint responsibility of the Defense Automated Printing Service, the Defense Logistics Agency, and DFAS.

Audit Objectives. The objective of the audit was to determine whether the FY 1997 Defense Automated Printing Service financial data, which were incorporated in the FY 1997 Defense Logistics Agency Defense Working Capital Fund Financial Statements, were presented fairly in accordance with the "other comprehensive basis of accounting" described in Office of Management and Budget Bulletin No. 94-01, "Form and Content of Agency Financial Statements," November 16, 1993, as modified by Office of Management and Budget Bulletin No. 97-01, "Form and Content of Agency Financial Statements," October 16, 1996. We also assessed management controls and compliance with laws and regulations.

Audit Results. For FY 1997, the Defense Automated Printing Service reported \$92.2 million of accounts receivable and \$142.6 million of accounts payable that were not traceable to supporting documentation. DFAS also made net adjustments of negative \$72 million to the Defense Automated Printing Service's Fund Balance With Treasury account that were not supported or reconciled to the accounting records. The adjustments resulted in a negative balance of \$17.6 million in the Fund Balance With Treasury account, which is normally a positive balance. Additionally, the \$33.3 million in Property, Plant, and Equipment that the Defense Automated Printing Service listed in its financial statements was understated. The understatement resulted when

none of the more than 200 real property facilities occupied by the Defense Automated Printing Service were reported. We did not estimate the amount of the understatement because management did not know the value of the facilities. As a result, the Defense Automated Printing Service financial data were not reliable and could not be used to make management decisions or to accurately present the consolidated financial statements of the Defense Logistics Agency.

Summary of Recommendations. We recommend that the Director, Defense Automated Printing Service establish, in coordination with DFAS, formal procedures to reconcile all financial data to supporting documents in accordance with DoD Regulation 7000.14-R, the "DoD Financial Management Regulation", establish procedures to report Defense Automated Printing Service real property, and reflect the Defense Automated Printing Service's financial reporting weaknesses on the annual statement of assurance. We also recommend that the Director, DFAS, maintain records of all adjustments; disclose in footnotes the extent and effect of summary adjustments to financial data used in the Defense Automated Printing Service financial statements; and develop usable subsidiary ledgers for the Defense Automated Printing Service to facilitate reconciliation of financial data.

Management Comments. The Deputy Director, Defense Logistics Agency concurred and will meet with DFAS to establish formal procedures to periodically reconcile financial data to support documents, identify and report facilities used in support of its operations, and report all known financial reporting weaknesses beginning with the FY 1998 Statement of Assurance. The Director, DFAS, did not comment on a draft of this report.

Audit Response. The comments from the Deputy Director, Defense Logistics Agency were responsive. We request the Director, DFAS, provide comments on the final report by November 23, 1998.

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Part I - Audit Results

Audit Background

Defense Automated Printing Service (DAPS). On October 1, 1996, DAPS became a separate business area within the Defense Logistics Agency (DLA) Defense Working Capital Fund (DWCF) (formerly the Defense Business Operations Fund [DBOF]). Before FY 1997, DAPS was a DBOF activity administered by the Navy and called the Defense Printing Service. The Defense Printing Service, established in April 1992 from the Navy Printing Service, consolidated the printing, duplicating, and document automation resources for DoD. In FY 1997, the Deputy Secretary of Defense changed its name to DAPS and placed it under DLA administration. For FY 1997, DAPS reported \$399.9 million in revenue and \$388 million in expenses.

Accounting Records. Accounting records for DAPS are maintained under the management of the Defense Finance and Accounting Service (DFAS) Cleveland Center, Cleveland, Ohio. The field level accounting work is performed by the DFAS Charleston Operating Location at Charleston, South Carolina, which is a subactivity of the DFAS Cleveland Center. Also, DAPS activities directly input data to accounting systems or submit data to DFAS Charleston for input. Before DAPS was established, the Defense Printing Service maintained its own accounting system, the Printing Resource Management Information System (PRMIS). During FY 1997, DFAS replaced PRMIS with a new accounting system for DAPS, the Defense Working Capital Fund Accounting System (DWAS).

DFAS provides accounting services for DAPS; the accuracy of information in financial systems and reported on the financial statements is the joint responsibility of DAPS and DLA. Preparation of the financial statements is the joint responsibility of DAPS, DLA, and DFAS.

Audit Objectives

The objective of the DLA financial statement audit was to determine whether the FY 1997 DAPS financial data, which were included in the DLA Working Capital Fund Financial Statements, were presented fairly in accordance with the "other comprehensive basis of accounting" described in Office of Management and Budget Bulletin No. 94-01, "Form and Content of Agency Financial Statements," November 16, 1993, as modified by Office of Management and Budget Bulletin No. 97-01, "Form and Content of Agency Financial Statements," October 16, 1996. We also assessed management controls and compliance with laws and regulations as applicable to the overall audit objective. See Part II, Appendix A, for a complete discussion of the scope, methodology, and management controls.

FY 1997 Financial Reporting by the Defense Automated Printing Service

For FY 1997, DAPS reported \$92.2 million of accounts receivable and \$142.6 million of accounts payable that were not traceable to supporting documentation. DFAS also made net adjustments of negative \$72 million to the DAPS Fund Balance With Treasury account that were not reconciled to the DAPS accounting records. The adjustments resulted in a negative balance of \$17.6 million in the Fund Balance With Treasury account, which is normally a positive balance. Additionally, the \$33.3 million in Property, Plant, and Equipment that the DAPS listed in its statements was understated. The understatements resulted when more than 200 real property facilities occupied by the DAPS were not reported. We did not estimate the amount of the understatement because management did not know the value of the facilities. These conditions occurred because data were transferred into a new accounting system without adequate controls. Also, data from multiple systems were used without reconciliation to supporting documents or to the primary DAPS accounting system. Additionally, DAPS management did not follow guidance for reporting Property, Plant and Equipment as capital assets. As a result, the DAPS financial data were not reliable, and could not be used to make management decisions. The DAPS financial position was not accurately reflected in the FY 1997 DLA Financial Statements.

Management Control Requirements

Office of Management and Budget (OMB) Circular No. A-123, "Management Accountability and Control," June 21, 1995, defines internal controls as "... the organization, policies, and procedures used by agencies to reasonably ensure that ... reliable and timely information is obtained, maintained, reported, and used for decision making." DoD has established key accounting requirements (KAR) No. 8, "Audit Trails," to help meet the requirements of OMB Circular No. A-123. KAR No. 8 requires that transactions be adequately supported with pertinent documents and source records. Also, the transactions must be traceable to the individual source records. DoD requires a test to ensure the traceability of transactions. DoD Regulation 7000.14-R, the "DoD Financial Management Regulation," volume 1, May 1993, "General Financial Management Information, Systems, and Requirements," chapter 2, "Conceptual Framework," requires "periodic verification of general ledger balances with related balances in subsidiary records, and ... periodic verification of the latter with related document files. . . ."

Accounting Requirements. DoD 7000.14-R, the "DoD Financial Management Regulation," volume 1, gives DoD policies for compliant accounting systems. The Regulation specifies 13 KARs with which accounting systems must comply. The Regulation also states that a material noncompliance with a KAR requires corrective action within a reasonable period. The KARs

with a KAR requires corrective action within a reasonable period. The KARs are a composite of requirements of the General Accounting Office (GAO), the Office of Management and Budget (OMB), the Department of the Treasury, and DoD.

System Controls. KAR No. 7, "System Controls (Fund and Internal)," requires adequate internal controls to prevent, detect, and correct errors and irregularities that may occur. These controls should include periodic reconciliations among recorded transactions, transaction summaries, and support records.

Audit Trails. KAR No. 8, "Audit Trails," requires that financial transactions be adequately supported with pertinent documents and source records. All transactions must be traceable to individual source records. A key test of the adequacy of an audit trail is whether tracing a transaction forward from the source or back from the result will permit verification of the amount recorded or reported.

Information and Accounting Systems

When the Navy was responsible for the administering the printing service, it developed the Printing Resource Management Information System (PRMIS) as a management information system in order to track project costs and outputs. The system was developed prior to the Chief Financial Officers Act and was not developed as an accounting system. However, the Navy Printing Service and the Defense Printing Service used the system for accounting and management reports until October 1997. The system was replaced because of recognized weaknesses.

PRMIS did not comply with the KARs and DoD and Government requirements for accounting and financial reporting. The DFAS Cleveland Center FY 1996 Annual Statement of Assurance disclosed that PRMIS was not in compliance with GAO accounting principles, standards, and related requirements and that DFAS Cleveland Center planned to replace the system.

New System. In December 1994, the Under Secretary of Defense (Comptroller) directed that PRMIS be replaced by a commercial off-the-shelf system. DFAS selected a system from the General Services Administration supply schedule. The system selected was the Integrated Financial Management Information System developed by Digital Systems Group, Warminster, Pennsylvania. DFAS named the system the Defense Working Capital Fund Accounting System (DWAS) and began implementing the system in FY 1997.

DWAS had a phased-in deployment that began in June 1997 and was completed in October 1997. It was fielded in 1 month increments at the DAPS business team offices located in Philadelphia, Pennsylvania; San Antonio, Texas; Pensacola, Florida; Charleston, South Carolina; and simultaneously in San Diego, California and at Headquarters, DAPS, Fort Belvoir, Virginia.

At the time of the audit, DFAS had not certified DWAS as compliant with requirements for Federal financial management and reporting; however, DFAS was reviewing the system to determine compliance. Unlike PRMIS, DWAS has the required standard general ledger, transaction-based general ledger, historical files, and audit trails.

Transfer of Accounting Data

DAPS Financial Reporting. DAPS produces but does not publish separate financial statements. Its financial information is consolidated into the financial statements of the DLA Working Capital Fund. In the footnotes to the financial data submitted for consolidation into the DLA financial statements, DAPS reported that "due to the difficulties DFAS encountered while implementing the new system, accounting reports were not available to DAPS at the end of the fiscal year. Thus, an audit to confirm the validity of the data reported could not be performed."

PRMIS Data Conversion. An audit trail did not exist because data were not adequately validated prior to being transferred to the new accounting system. During FY 1997, DAPS financial data (for example, revenue, expenses, cash, receivables, and payables) were transferred from one accounting system PRMIS, to another, DWAS. DWAS had a phased-in deployment that began in June 1997 (9 months after the beginning of FY 1997) and was completed in October 1997 (1 month after the beginning of FY 1998). It was fielded in one month increments to the five DAPS business team offices. As a result, most FY 1997 accounting transactions were entered into PRMIS by DAPS personnel and converted to DWAS. DAPS personnel were responsible for validating the PRMIS data before conversion to DWAS. DAPS business team managers were instructed by Headquarters, DAPS, to review the data in PRMIS and make the necessary adjustments so that only valid data would be converted to DWAS.

DAPS did not have records to support the data converted to DWAS. Our review of the conversion process showed that DAPS was not able to quantify the number of adjustments, the dollar value of the adjustments, or the summary affect on the accounts. Because the change of accounting systems represented a major change in accounting activity, the conversion process was subject to the principle of full disclosure. The conversion process should have been shown in the footnotes to the DAPS financial data. When DAPS management issued conversion instructions to subordinate activities, instructions to summarize the change data were not provided. Data from PRMIS were converted to DWAS with little or no evidence of verification or reconciliation to the original supporting documents. This internal control was not included in the conversion instructions. These data became the beginning balances for the accounts in DWAS and the accuracy of the data entered was doubtful because of the lack of reconciliation. DAPS personnel stated, and our review of the documentation confirmed, that before conversion, DAPS did not have a procedure for periodic reconciliation of accounting data to the original support documents. Also, DAPS personnel stated, and our review of documentation confirmed, that DAPS did not compare individual transactions or summary data to the original

support documents. Since the data were not verified, their validity was in doubt. Also, because accounting reports and ledgers were not available, we could not verify the reported balances.

Accounts Payable and Receivable. DAPS personnel did not receive usable detail reports of these accounts from DFAS after the conversion of systems. This prevented DAPS personnel from reconciling of the accounts to supporting documents. As of May 1998, DAPS was not able to obtain usable subsidiary data on the accounts. As a result, the net balances of \$92.2 million for accounts receivable and \$142.6 million for accounts payable have not been reconciled and are questionable. The Statement of Financial Position showed \$100.4 million for Accounts Receivable from Federal Entities and a negative \$8.2 million as Accounts Receivable from Non-Federal Entities. Further, the statement reflected \$105.2 million for Federal Payables and \$37.4 million in Non-Federal Payables. However, we could not determine, and DAPS and DFAS could not demonstrate the amounts due from its customers (accounts receivable) or what the amounts DAPS owes to others (accounts payables).

Multiple Systems

FY 1997 Financial Report Data Sources. The DAPS financial statement data were the result of combining information from five sources. Three of the sources were accounting software systems that were not integrated.

- The first source was reports from the old PRMIS system for two DAPS groups (headquarters and the Western business team) not yet converted to DWAS.
- The second was a data extract generated by the DWAS contractor for the rest of the DAPS activities, because the DWAS did not generate a trail balance.
- The third automated source was funds collections and disbursements data from a DFAS Cleveland system (Industrial Funds Cash Disbursements and Receipts System).
- The fourth source was adjustments to accounts based upon conversations between DFAS Charleston accounting office personnel who supported DAPS, and DFAS Charleston DWAS program management office personnel.

The data from these four sources were combined into a report sent to the DFAS Cleveland Center. The fifth source was further adjustments to fund collections and disbursements (Fund Balance With Treasury) and related accounts by the DFAS Cleveland Center. The adjustments were a result of the combination of data from DFAS Cleveland Center's Central Expenditure Reimbursement Processing System Report and DFAS Indianapolis Center's Cash Management

Report. These adjustments were made to replace the DAPS accounting system collection and disbursement records (Fund Balance With Treasury) with the combined data from DFAS Cleveland and DFAS Indianapolis.

Data Support. We attempted to validate the data combinations and adjustments. However, adequate documentation was not available and we were not able to verify the accuracy of the combined data. While there were hard copy reports for the PRMIS information, the system was terminated and we could not verify the reports. We were unable to determine the validity of the data in the DWAS extract because DWAS did not have a trial balance report available and we did not have access to data in the system. DFAS Charleston did not receive a DWAS Summary Trial Balance Report from the DWAS system until after the FY 1997 final DFAS Charleston submission to DFAS Cleveland had been sent.

Charts of Accounts. DFAS used multiple charts of accounts for DAPS financial data. A chart of accounts is the basis of an accounting system; it lists and classifies the accounts and describes the purpose and content of each. The U.S. Government has established an official chart of accounts, the U.S. Government Standard General Ledger (USGSL). DoD has established a chart of accounts, the DoD Standard General Ledger (SGL), which is based on the USGSL. The DWAS data were in the DoD adaptation of the USGSL chart of accounts. Due to multiple conversions, the data for DAPS financial reports were not in the DoD SGL. A Navy chart of accounts, which did not conform to the DoD SGL, was used to report DAPS financial data.

Multiple Account Crosswalks. To convert DWAS data, a software program was run against the DWAS data. The DWAS data was stored in the DoD SGL format; however, the extract produced a listing in a Navy chart of accounts format. This occurred because all other sources of data were in the Navy chart of accounts format and had to be combined with the DWAS extract. A conversion map was not available to show the data that were transferred from the DoD SGL to the Navy chart of accounts. As a result, we could not determine what data was reflected in which accounts.

The PRMIS data, which were in the Navy chart of accounts format, and the DWAS converted data were combined into a file with the Navy chart of accounts. The file was forwarded to the DFAS Cleveland Center. The DFAS Cleveland Center processed the file and converted it into the DoD SGL chart of accounts for preparing the financial statements. Data integrity is questionable because of the repeated conversions. Also, there was a lack of audit trails for the conversion of DWAS data to Navy SGL data.

Unsupported System Adjustments. The DFAS Cleveland Center made a net total of negative \$72 million of unsupported adjustments to the DAPS accounting system's Fund Balance With Treasury account, which had a preadjustment balance of \$54.4 million. The adjustment resulted in a negative \$17.6 million balance. The DFAS Cleveland Center used the combination of data from the Central Expenditure Reimbursement Processing System report and the DFAS Indianapolis Center's Cash Management Report to arrive at the reported negative \$17.6 million Fund Balance With Treasury.

The negative \$72 million net difference was not reconciled to the DAPS accounting system's Fund Balance With Treasury account. DFAS personnel did not use the DAPS Fund Balance With Treasury from the DAPS accounting system because DoD guidance directed them not to do so. However, the guidance did not prohibit reconciliation to the client's data or prohibit adequately providing annotation in footnotes to the financial statements. The \$72 million was reflected on the Statement of Financial Position as a negative Other Federal (Intragovernmental) Liability. The problem was perpetuated because DFAS Cleveland Center records and the PRMIS records had not been reconciled in recent years, and when DAPS sites converted to DWAS, the unreconciled balances were transferred from PRMIS to DWAS.

Similarly, in 1994, the IG, DoD, reported that collection and disbursement data compiled by DFAS were not reconciled to DLA accounting records. The IG, DoD, audited the FY 1993 DLA financial statements and found internal control deficiencies in the Fund Balance With Treasury account. Data collected by DFAS were not reconciled to DLA accounting records, although significant variances existed between the two sets of records, and disclosures on statements of cash flow and footnotes were inadequate.

The IG, DoD, issued Report No. 94-159, "Fund Balance With Treasury Accounts on the FY 1993 Financial Statements of the Defense Logistics Agency Business Areas of the Defense Business Operations Fund," June 30, 1994. The IG, DoD, recommended that DFAS establish adequate audit trails and reconciliations between Treasury reporting systems and DFAS clients' accounting records. DFAS did not comment on the report. Our followup audit, Report No. 98-148, "Internal Controls and Compliance With Laws and Regulations for the FY 1997 Financial Statements of the Defense Logistics Agency Working Capital Fund," June 5, 1998, reported that previously identified deficiencies in collection and disbursement data were not corrected. Therefore, we are not making a recommendation in this report.

Property, Plant, and Equipment

The FY 1997 financial statements reported \$33.3 million in Property, Plant, and Equipment. This balance was understated because the Property, Plant, and Equipment account did not reflect the real property used by the business activity.

Real Property. DAPS did not report financial data on the real property assets it was using. DoD Regulation 7000.14-R, the "DoD Financial Management Regulation," volume 11B, "Reimbursable Operations, Policy and Procedures -- Defense Business Operations Fund (DBOF)," December 1994, states, "Capital assets used by a DBOF (WCF) activity in providing goods and services must be recognized in the property and financial records of that activity." None of the more than 200 sites used by DAPS were recognized on the DAPS financial records. For example, at the Southeastern business team, the main production site occupied an entire building. The building had a cost of about \$1.1 million. Almost all DAPS buildings were in use based on agreements with installations.

DAPS resource management personnel stated that since DAPS did not own the real property, DAPS was not required to recognize it. However, the real property provides a future benefit to the entity; therefore, the property should be shown on the financial statements.

Annual Statement of Assurance

On the DAPS FY 1997 Annual Statement of Assurance, DAPS management did not report the financial weaknesses such as the problems with the accounting systems. DAPS managers did not believe that they were responsible for reporting the accounting systems weaknesses because DAPS did not own the accounting systems. The managers believed that DFAS was responsible for reporting such weaknesses. DoD Regulation 7000.14-R, the "DoD Financial Management Regulation," volume 6, "Reporting Policy and Procedures," February 1996, chapter 2, "Departmental Financial Reports, Roles and Responsibilities," states that DFAS and its clients, the operating entities such as DAPS, share responsibility for financial reporting and the integrity of financial data. Known weaknesses are also a joint responsibility for reporting and correcting.

Other Matters of Interest

Reporting responsibility for the DAPS business area was expected to be transferred from DFAS Cleveland Center to DFAS Columbus Center, Columbus, Ohio. As of July 1998, the transfer had not occurred. Columbus Center personnel stated that they were reluctant to absorb responsibility for DAPS accounting until the DWAS was fully functioning. Two factors affected their position. They were not in the planning and acquisition cycle for DWAS. Also, Charleston Operating Location was not under their management structure.

Recommendations for Corrective Action

1. We recommend that the Director, Defense Automated Printing Service:
 - a. Establish, in coordination with the Defense Finance and Accounting Service, formal procedures to periodically reconcile all financial data to support documents in accordance with the DoD Regulation 7000.14-R, the "DoD Financial Management Regulation."
 - b. Establish the procedures required by DoD Regulation 7000.14-R, the "DoD Financial Management Regulation," for identifying and reporting on financial statements the real property used in support of the Defense Automated Printing Service operations.

c. Report all known financial reporting weaknesses on the Annual Statement of Assurance.

Management Comments. The Deputy Director, Defense Logistics Agency concurred and stated that DAPS will meet with DFAS to establish formal procedures to periodically reconcile all financial data to support documents in accordance with regulations by November 1998. DAPS has identified and will report facilities used in support of operations that meet DoD FMR reporting criteria. Also, DAPS will report all known financial reporting weaknesses beginning with FY 1998 Statement of Assurance.

2. We recommend that the Director, Defense Finance and Accounting Service:

a. Establish audit trails, in accordance with Key Accounting Requirement No. 8, "Audit Trails," for all adjustments to the Defense Automated Printing Service financial statements, and fully disclose in the footnotes to the financial statements the extent and effect of summary adjustments.

b. Develop, in coordination with the Defense Automated Printing Service, usable subsidiary ledgers to facilitate the reconciliation of financial data.

Audit Response

The Director, Defense Finance and Accounting Service, did not comment on a draft of this report. We request that the Director, Defense Finance and Accounting Service, provide comments on this final report.

Part II - Additional Information

Appendix A. Audit Process

Scope and Methodology

Because this is the first audit of DAPS by the IG, DoD, and because a new accounting system is being fielded, it was not feasible to perform a financial statement audit as defined by Government auditing standards. Also, DAPS disclosed in footnotes to its financial data that:

“Due to difficulties DFAS encountered while implementing the new system, accounting reports were not available to DAPS at the end of the fiscal year, thus, an audit to confirm the validity of the data reported could not be performed.”

This financial-related audit was conducted from October 1997 through June 1998 in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD. We reviewed:

- the accounting system conversion from PRMIS to DWAS,
- accounting system compliance with DoD regulations,
- preparation of the financial statements,
- prior audit reports,
- accounting reports, and
- supporting details for FY 1997 data.

We also reviewed financial data on the Fund Balance With Treasury, Accounts Receivable, Accounts Payable, and Property, Plant, and Equipment as of the end of FY 1997.

We made a limited assessment of the reliability of computer-processed data. We did not have access to the automated financial systems to verify reported transactions and summary results in the systems. We did not use statistical sampling procedures.

Contacts During the Audit. We visited or contacted individuals and organizations within DoD. Further details are available on request.

DoD-wide Corporate-Level Government Performance and Results Act (GPRA) Goals. In response to the GPRA, the DoD has established 6 DoD-wide corporate-level performance objectives and 14 goals for meeting these objectives. This report addresses issues related to achievement of the following objective and goal.

- **Objective:** Fundamentally reengineer the Department and achieve a 21st century infrastructure.
- **Goal:** Reduce costs while maintaining required military capabilities across all DoD mission areas. (DoD-6)

DAPS had established performance measures. However, the measures were not parallel with the DoD objectives and goals. DAPS performance measures and goals addressed operating efficiency and costs per unit, which depend on a reliable financial data system. In order to reduce costs, reengineer and to make management decisions, accurate and reliable financial data are required. Financial data for DAPS were not reliable. Therefore, we did not evaluate the DAPS performance measures and goals.

DoD Functional Area Reform Goals. Most major DoD functional areas have also established performance improvement reform objectives and goals. This report pertains to achievement of the following Financial Management functional area objectives and goals.

- **Objective:** Consolidate finance and accounting operations.
- **Goal:** Consolidate and standardize financial systems. (FM-2.1)
- **Goal:** Reduce and improve accounting systems. (FM-2.2)
- **Objective:** Strengthen internal controls.
- **Goal:** Improve compliance with the FMFIA. (FM-5.3)

General Accounting Office (GAO) High-Risk Areas. GAO has identified several high-risk areas in DoD. This report provides coverage of the Defense Financial Management and Information Management and Technology high-risk areas.

Management Control Program

DoD Directive 5010.38, "Management Control Program," August 26, 1996, requires DoD organizations to implement a comprehensive system of management controls that provides reasonable assurance that programs are operating as intended and to evaluate the adequacy of the controls. Procedures for implementing the Directive are outlined in DoD Instruction 5010.40, "Management Control Program Procedures," August 28, 1996.

Scope of Review of the Management Control Program. We reviewed the adequacy of DPAS and DFAS management controls over the accounting and reporting for DAPS. We included tests of management controls considered necessary. Specifically, we reviewed management controls established to ensure that reliable and complete accounting data were entered into financial systems and that documentation was retained to support reported amounts.

Adequacy of Management Controls. We identified material management control weaknesses for DAPS and DFAS, as defined by DoD Instruction 5010.40. DAPS and DFAS controls over financial reporting were not adequate to ensure the statements were accurate and fully supported. DAPS did not develop the management controls necessary to ensure verification of the financial data in DWAS. DFAS did not develop the controls to document and report all adjustments to data on the financial statements. Further, DFAS did not report any weaknesses for DWAS, such as not being certified as meeting Federal financial management and reporting requirements. Recommendation 1.a. if implemented, will establish internal controls over the DAPS validation of financial data, and Recommendation 1.b. will result in improved accountability over Property, Plant, and Equipment, and Recommendation 1.c. will result in disclosure of DAPS' progress toward effective internal controls over financial data. Recommendation 2.a. will provide DFAS with a management trail to support summary adjustments to the DAPS financial statements. Recommendation 2.b. will provide both DAPS and DFAS with management trails to facilitate the validation of financial data.

We identified material management control weaknesses. Therefore, a copy of this report will be provided to the senior officials in charge of management controls for DAPS, DLA, and DFAS.

Adequacy of Management's Self-Evaluation. Financial reporting is the joint responsibility of DLA, DAPS, and DFAS. Each organization is required to evaluate its contribution to the financial statements. As a result, both the originating activity for accounting data (DPAS) and the presenter of the financial statements (DLA) are required to evaluate their procedures and systems for providing financial data to DFAS. Also, the recording activity, DFAS, is required to evaluate its systems, processes, and procedures for providing data for the financial statements. The evaluations by DAPS and DFAS were not adequate. DAPS did not identify its financial reporting weaknesses because they believed that financial reporting was the responsibility of DFAS. DFAS did not report on DWAS because it was not yet an accepted system.

DLA FY 1997 Annual Statement of Assurance. The DLA FY 1997 Annual Statement of Assurance included DAPS, but did not report any material weaknesses for DAPS.

DAPS FY 1997 Annual Statement of Assurance. DAPS did not identify accounting system weaknesses in the FY 1997 Annual Statement of Assurance. DAPS managers did not believe that they were responsible for reporting the accounting systems weaknesses because DAPS did not own the accounting systems. The managers believed that DFAS was responsible for reporting such weaknesses.

DFAS Cleveland Center's Annual Statement of Assurance. DAPS' financial data were accumulated by the DFAS Cleveland Center. In the FY 1996 Annual Statement of Assurance for the management control program, DFAS Cleveland Center identified and reported material weaknesses in 46 of the 57 finance and accounting systems it operated, including PRMIS. DFAS Cleveland Center reported that these 46 systems were not in compliance with General Accounting Office accounting principles, standards and related requirements.

For FY 1997, DFAS Cleveland Center did not disclose system weaknesses in their FY 1997 Annual Statement of Assurance, however; the system weaknesses, including PRMIS, were identified in the DFAS Cleveland Center Chief Financial Officer's Financial Management 5-Year Plan. However, DFAS did not report on whether the new system, DWAS, met Federal financial management reporting requirements.

Summary of Prior Coverage

In the last five years, no audit reports were issued on the DAPS financial statements. The Naval Audit Service performed financial audits of the Defense Printing Service, the predecessor of DAPS; however, they did not review the Defense Printing Service for FY 1995 or 1996. Other reports related to the DLA financial statements include the following:

- IG, DoD, Report No. 98-148, "Internal Controls and Compliance With Laws and Regulations for the FY 1997 Financial Statements of the Defense Logistics Agency Working Capital Fund," June 5, 1998.
- IG, DoD, Project No. 8FJ-2002, "Audit Opinion on the Defense Logistics Agency Working Capital Fund Financial Statements for FY 1997," February 27, 1998.
- IG, DoD, Report No. 94-159, "Fund Balance With Treasury Accounts on the FY 1993 Financial Statements of the Defense Logistics Agency Business Areas of the Defense Business Operations Fund," June 30, 1994.

Appendix B. Report Distribution

Office of the Secretary of Defense

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Deputy Comptroller (Program/Budget)
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Director, Defense Finance and Accounting Service, Cleveland Center
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Senate Committee on Armed Services
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House Committee on Government Reform and Oversight
House Subcommittee on Government Management, Information, and Technology,
Committee on Government Reform and Oversight
House Subcommittee on National Security, International Affairs, and Criminal
Justice, Committee on Government Reform and Oversight
House Committee on National Security

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Part III. Management Comments

Defense Logistics Agency Comments



DEFENSE LOGISTICS AGENCY
HEADQUARTERS
8725 JOHN J. KINGMAN ROAD, SUITE 2533
FT. BELVOIR, VIRGINIA 22060-6221

REPLY
REFER TO


DDAI

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING
DEPARTMENT OF DEFENSE

SUBJECT: OIG Draft Report, *"FY 1997 Financial Reporting by the Defense Automated
Printing Service,"* (Project No. 8FJ-2002.04)

This is in response to your August 31, 1998 request. If you have any questions,
please contact Ms. Annell Williams, 703-767-6274.

Encl


JEFFREY GOLDSTEIN
Chief (Acting), Internal Review Office

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Defense Logistics Agency Comments

Subject: FY 1997 Financial Reporting by the Defense Automated Printing Service
Project No. 8FI-2002.04

Recommendations:

1. DoD-IG recommends that the Director, Defense Automated Printing Service:

- a. Establish, in coordination with the Defense Finance and Accounting Service, formal procedures to periodically reconcile all financial data to support documents in accordance with the DoD 7000.14-R, the "DoD Financial Management Regulation."

DAPS Reply: Concur. DAPS will initiate meeting with DFAS for the purpose of establishing formal procedures to periodically reconcile all financial data to support documents in accordance with regulations by November 1998.

- b. Establish the procedures required by DoD 7000.14-R, the "DoD Financial Management Regulation," for identifying and reporting on financial statements the real property used in support of the Defense Automated Printing service operations.

DAPS Reply: Concur. DAPS has identified and will report the ten facilities used in support of its operations which meet the DoD FMR reporting criteria.

- c. Report all known financial reporting weaknesses on the Annual Statement of Assurance.

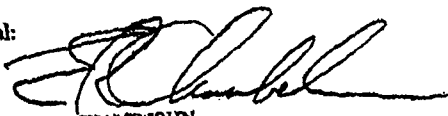
DAPS Reply: Concur. DAPS will report all known financial reporting weaknesses starting with the FY 1998 Statement of Assurance.

Action Officer: Richard DeNeane, DAPS

Review/Approval: Richard DeNeane, Director, Corporate Resources, DAPS

Coordination: Annell Williams, DDAI

DLA Approval:


E.R. CHAMBERLIN
Rear Admiral, SC, USN
Deputy Director

Audit Team Members

This report was prepared by the Finance and Accounting Directorate, Office of the Assistant Inspector General for Auditing, DoD.

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